

THE OHIO USE TAX

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The economic depression has caused the states of the federal union to seek varied and new sources of revenue. In more than half the states the sales tax in some form or other has come to be a substantial part of the fiscal system. In Ohio a sales tax law has been in effect since December 13, 1934, although the actual levy did not take place until January 27, 1935. The sales tax law has now been extended until March 31, 1937, the original act containing an expiration date of December 31, 1935.¹

In the first year of sales tax administration, Ohio found, as have other states, that Ohio merchants and vendors could not compete with out-of-the-state vendors who, under the protection of the interstate commerce clause of the Federal Constitution, were selling commodities tax free to Ohio consumers. Ohio's experience has not been unique. It has been more or less true in all the states imposing the sales tax. Washington, California, and Oklahoma have attempted to reach the problem through a Use Tax. Ohio has now decided to utilize the same instrument. The Ohio Use Tax was enacted by the General Assembly on December 20, 1935, and signed by the Governor, December 23, 1935, and takes affect on January 1, 1936.

A very excellent pronouncement upon the legal aspects of use taxation will be found in the *North Carolina Review*. (Perkins, *The Sales Tax and Transactions in Interstate Commerce*, 12 N. C. L. Rev. 99, 1933.)

The primary reason for the commerce clause of the Federal Constitution was to make possible the free movement of

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¹ See: *Economic and Legal Aspects of the Sales Tax*, Carlton S. Dargusch, 1 OHIO ST. L. J. 192 (1935)—Ed. note.

interstate commerce. That the commerce clause of the Constitution has well served its purpose is more than well established by history. The tendency, however, has now been to impair the movement of domestic commerce and the need has grown so great that some solution had to be found if sales taxes were to continue, in view of the tax threat to domestic commerce.

The solution is not to grant special privileges to local business, but to take away those special privileges from property which has moved in interstate commerce. The obstacles to such a solution are found in:

1. Repeated pronouncements by the Supreme Court, prohibiting state taxation of interstate commerce. *Robbins v. Shelby Taxing District*, 120 U.S. 489, 7 S. Ct. 592, 30 L. Ed. 694 (1887); *Brennan v. Titusville*, 153 U.S. 289, 14 S. Ct. 829, 38 L. Ed. 719 (1894); *Rearick v. Pennsylvania*, 203 U.S. 507, 27 S. Ct. 159, 51 L. Ed. 295 (1906); *Crenshaw v. Arkansas*, 227 U.S. 389, 33 S. Ct. 294, 57 L. Ed. 565 (1913); *Real Silk Hosiery Mills v. Portland*, 268 U.S. 325, 45 S. Ct. 525, 69 L. Ed. 982 (1925).

2. Restrictions of a state's collection functions to its own limits and the fact that a state has no extra-territorial jurisdiction for taxation purposes. *Standard Oil Co. v. California*, 291 U.S. 242, 54 S. Ct. 381, 78 L. Ed. 775 (1934); *Moore v. Mitchell*, 281 U.S. 18, 50 S. Ct. 175, 74 L. Ed. 673 (1930).

The Ohio Use Tax Law tries to reach this situation by placing its own merchants on the same basis as those merchants out of the state. It is patterned after the Ohio Sales Tax Law and the tax is imposed at the same rate and, when collected by the party making the sale, the collection is by means of prepaid tax receipts. The tax is levied upon the storage, use or other consumption of tangible personal property purchased from vendors for storage, use or consumption in this state.

If a comparison of the two Acts were to be made, it would be found that the only substantial difference is that the one

imposes a tax upon each retail sale of tangible personal property made in the State of Ohio, while the other imposes a tax on the storage, use or consumption of tangible personal property and exempts from the tax property the sale of which is subject to the sales tax.

The primary responsibility for the payment of the use tax is placed on the consumer who stores, uses, or otherwise consumes the tangible personal property, and it is extinguished only by payment.

The mechanics and operation of the Use Tax Act are the same as the Sales Tax Act, in those cases where the seller of the tangible personal property has registered with the Tax Commission. In such cases the seller, or vendor, will obtain prepaid tax receipts and collect the tax from consumers in the same manner and at the same time as in the case of the Sales Tax Act. In case the vendor, from whom the consumer purchases, does not collect the tax for the state, it is the duty of the latter to file a return with the State Tax Commission and pay the proper amount of tax. This return is to be made at quarterly periods, or at such other times as the Commission may prescribe.

The theory on which the use tax is based is that the state protects the right to use tangible personal property which a consumer may own and may, therefore, tax for the protection granted. It must be borne in mind that a use tax is not in the nature of a property tax, but is a form of excise tax.

It will be seen that the entire purpose of the Use Tax Law is to supplement the Sales Tax Law by imposing upon those subject to it an equivalent tax burden to that levied by the Sales Tax Law, with substantially identical exemptions in each case. For that reason, the Use Tax Law limits the levy to property purchased for storage, use, or consumption within the State of Ohio.

The courts have recognized that a tax may be imposed upon the use as well as upon the sale of a commodity. *Bowman v. Continental Oil Co.*, 256 U.S. 642, 648, 41 S. Ct. 606, 65 L.

Ed. 1139 (1921), and *Hart Refineries v. Harmon*, 278 U.S. 499, 49 S. Ct. 188, 73 L. Ed. 475 (1929). In the latter, the court, at page 501, stated:

Interstate transportation having ended, the taxing power of the state in respect of the commodity which was the subject of such transportation, may, so far as the commerce clause of the federal court is concerned, be exerted in any way which the state constitution and laws permit, provided, of course, it does not discriminate against the commodity because of its origin in another state. That, under such circumstances, a tax may be imposed upon the use as well as upon the sale of the commodity in domestic trade, without coming into conflict with the commerce clause, was specifically determined in *Bowman v. Continental Oil Co.*

Assuming that it has been established that the use of tangible personal property within a state can properly be subjected to tax, the next question is that of discrimination, when such tax is imposed on tangible personal property which has been shipped into the state in interstate commerce. It is fundamental, of course, that the states cannot single out commodities which have been shipped in interstate commerce and discriminate against such commodities in favor of those shipped and sold in intrastate commerce.

In view of the fact that the Use Tax Act exempts from the tax thereby imposed the use of articles which were purchased in such manner that the Ohio Sales Tax has been paid, it would appear that there is discrimination. In effect, the use tax applies practically in only those cases where the merchandise was purchased in interstate commerce, as in most other cases the sales tax would be applicable. It would likewise appear that the state is attempting to do indirectly that which it cannot do directly; i.e., impose a burden on interstate commerce. In connection with these two apparent criticisms of the use tax, it is interesting to note the decision of the Supreme Court of the United States in the case of *Gregg Dyeing Co. v. Query et al.*, 286 U.S. 472, 52 S. Ct. 631, 76 L. Ed. 1232 (1932). In that case the plaintiff attacked the validity of the South Carolina

statute requiring every person, firm, or municipality, which imported gasoline and kept it in storage for future use in that state, to pay a license tax of six (6) cents per gallon. The statute in question exempted from the application of the tax any gasoline which had been subjected to the payment of the license taxes imposed by other statutes of the state. The plaintiff, the Gregg Dyeing Co., purchased gasoline in bulk from dealers outside the state of South Carolina and had it shipped into the state to the plaintiff's plant, where it was unloaded and stored until needed for use. It was contended that the tax was a burden on interstate commerce and that it was discriminatory in that a refinery maintained by the Standard Oil Company did not pay a tax on gasoline which it produced and stored, or imported and stored in South Carolina for purpose of sale.

The Supreme Court of the State of South Carolina upheld the constitutionality of the act in question for the reason that it was no burden on interstate commerce, for the act operated only after the commodity had been severed from its interstate character and had become at rest as a general mass of property in the state. It was pointed out further that the tax was an excise tax and not a property tax and that all oil companies in South Carolina were required to pay a tax on gasoline sold or used in the state. The state court held that the act in question was not discriminatory for it was complementary to the other statutes of South Carolina under which there was assessed the gallonage tax on gasoline and other petroleum products.

The Supreme Court of the United States affirmed the decision of the state court and in the opinion pointed out that there was no demand in the Federal Constitution that an act passed by a state legislature must be constitutional "within its four corners." The constitutionality of a state taxing scheme is to be determined by substance rather than by form, and when the supreme court of the state has held that two or more statutes may be taken together, the Supreme Court of the United States will accept that conclusion as if written into the statutes

themselves. The court in this case likewise ruled that the same consideration, with respect to discriminations, applied to the claim that a statute violates the equal protection clause of the Fourteenth Amendment.

In applying the rule laid down by the Supreme Court in the case of *Gregg Dyeing Co. v. Query et al* to the Ohio situation, we are led to believe that the use tax is constitutional for it is not discriminatory, does not deny equal protection of the laws and does not place a burden on interstate commerce.

Reading and construing the Sales Tax Act and the Use Tax Act together, we find that the consumer of tangible personal property must pay exactly the same amount of tax, regardless of whether the property consumed is purchased within or without the state.

Critics of the use tax point out that after granting such tax is constitutional and may be levied legally, the administration problems in connection therewith will be numerous and complicated. The chief obstacle in administration is the fact that in many cases collection must be made from consumers who are placed under the responsibility of payment of the tax. Parties liable for the tax have a good chance of evading it, due to their numbers. This obstacle is overcome in large part by requiring retailers of tangible personal property to collect the tax as agents of the state. In connection with this matter, it should be noted that there are two classes of vendors who will make sales in interstate commerce: first, those who maintain retail establishments or agents in the state; and second, those who sell direct and do not maintain agents or retail establishments.

The Act requires that those vendors who have agents or places of business within the State of Ohio must register with the Tax Commission and collect the tax on all sales to the consumer, even though the shipment may originate in another state. That the state has this power to require retailers, maintaining places of business in a state, to collect an excise tax, even though a portion of their sales may involve shipments in interstate com-

merce, was settled in the case of *Monamotor Oil Company v. Johnson*, 292 U.S. 86, 54 S. Ct. 575, 78 L. Ed. 1141 (1934):

The appellant, however, says that the state officials have required it to report and to pay tax on shipments made from Oklahoma direct to dealers in Iowa, who are appellant's customers, and that in respect of such transactions the burden on interstate commerce is obvious. But if the gasoline so imported is intended to be used in Iowa for motor vehicle fuel, it is subject to the tax. If it is not so used by the appellant's customer, or by the purchaser at retail, either may obtain a refund of the tax collected by the appellant and remitted to the state. The statute obviously was not intended to reach transactions in interstate commerce, but to tax the use of motor fuel after it had come to rest in Iowa, and the requirement that the appellant as the shipper into Iowa shall, as agent of the state, report and pay the tax on the gasoline thus coming into the state for use by others on whom the tax falls imposes no unconstitutional burden either upon interstate commerce or upon the appellant.

As to those retailers who do not maintain places of business within the State of Ohio and who, therefore, cannot be forced to collect the tax as they are outside the jurisdiction of Ohio, it is believed that many will voluntarily register with the Tax Commission and collect the tax so that their customers may not be harassed and placed under the inconvenience of making out and filing returns with the state.

If the use tax is finally held to be constitutional, as we confidently expect it to be, the problems of unfair competition attributable to interstate commerce will largely be eliminated, and Ohio's merchants will be relieved of the discrimination which they have been compelled to bear upon the domestic commerce of this state.